UNITED STATES OF AMERICA
BEFORE THE
DEPARTMENT OF ENERGY

Interstate Electric Transmission System; Electric Reliability Issues	)

COMMENTS & ANSWERS OF
ENRON POWER MARKETING, INC.

Pursuant to the Department's November 20, 2000, Notice of Inquiry ("NOI"), Enron Power Marketing, Inc., ("EPMI") hereby submits its comments and answers to the questions that the Department asked in the NOI.

I.
EXECUTIVE SUMMARY

A 1998 report to the Department correctly concluded that new policies and institutions would need to be developed to maintain the security[1] of the bulk power system as it continues to evolve from franchise monopolies to competition. Specifically, a competitive bulk power market needs enforceable operating standards designed to secure the system. The Department should proceed with a rule-making directing the Federal Energy Regulatory Commission's ("FERC") to implement the needed policies and institutions.

[1]In these comments and the answers that follow, EPMI recognizes that reliability of the bulk power system stands on two legs. On the one hand, a reliable bulk power system must have access to power supplies adequate to meet demand. This is generally referred to simply as the *adequacy* aspect of reliability. On the other hand, reliability also depends on *security*, which requires that an operator is able to prevent the interconnected transmission system from (1) becoming thermally overloaded, (2) unstable on AC transmission lines, and (3) suffering voltage collapse. EPMI understands the Department's focus in this NOI to be on new policies and structures needed to maintain security. At the same time, however, it would be unwise to lose sight of the fact that managing security in different ways, can affect price signals that are needed to inform decisions to invest in generation adequacy. Policies and structures that achieve security without distorting the power supply market forces should be the goal and is what EPMI proposes in the answers below.

Legislation to create a private standard setting organization with enforcement authority was proposed but not enacted in the 106th Congress. In the absence of such legislation, the institution through which standards should be developed and enforced are regional transmission organizations ("RTOs"), as proposed in FERC Order No. 2000[2], and which are scheduled to be in place by December 15, 2001. The standards developed and proposed by RTOs for maintaining security, if accepted by FERC, can be included in RTOs' transmission tariffs and thereby made enforceable by FERC. Pending RTO formation throughout the contiguous states, the Department should direct FERC to ask the North American Electric Reliability Council ("NERC") to propose reliability standards that NERC believes must be enforceable in order to maintain security. Those standards that FERC accepts as just and reasonable and not unduly discriminatory under the Federal Power Act ("FPA"), should be made part of NERC's tariff on file with FERC, and thereby made enforceable in actions at FERC.

In its rule-making, the Department should direct FERC to take all steps necessary to guarantee full RTO participation by all transmission owning public utilities ("TOPU") that are subject to FERC jurisdiction under the FPA. FERC should also be directed to ensure that the RTOs are fully independent and offer service on the interstate grid to all users on a basis that is transparently equal and nondiscriminatory, as more fully set out below.

[2] *Regional Transmission Organizations*, Order No. 2000, [1996 - 2000 Regs. Preambles] III F.E.R.C. Stats. & Regs. ¶ 31,089 (2000), *order on reh'g*, Order No. 2000-A, III F.E.R.C. Stats. & Regs. ¶ 31,092 (2000), *appeal docketed sub nom. Public Utility District No. 1 of Snohomish County, Washington v. FERC*, Nos. 00-1174, *et al.*, (D.C. Cir. April 24, 2000).

II.
COMMENTS

EPMI commends the Department for its timely focus on enforceable reliability standards for the competitively restructured electric power industry. The NOI quotes from the 1998 Report of the Secretary's Advisory Board's Task Force on Electric System Reliability, which alerted the industry to the need for new policies and institutions to maintain the security of the bulk power system as the industry transitions from the era of cooperating franchise monopolists to one of merchants, without captive customers, competing for sales, both at wholesale and at retail. The industry's failure to act promptly on the Task Force's warning has contributed to the power shortages and extreme price volatility that certain regions have experienced in the two years since the report's issuance. Through this NOI, the Department, together with FERC, can proceed with a rule-making to help the industry develop the new policies and structures needed to maintain security in a competitively restructured industry.

Since its founding in 1968, the NERC and its regional councils (currently ten) have set reliability standards in the form of policy guidelines for the industry. In the historical industry structure of franchise utility monopolies with captive customer bases, these voluntary guidelines were adhered to voluntarily, and NERC neither had nor appeared to need the ability to enforce compliance or sanction noncompliance. That structure has been displaced by power supply competition. For reasons identified in the NOI and explained more fully in EPMI's responses to the Department's questions, full compliance with voluntary standards can no longer be taken for granted. Two legal hurdles stand in the way of mandating compliance with reliability standards in a competitive power industry. First, neither NERC nor its regional councils can make the standards mandatory and enforce them by punishing violations without exposing themselves to liability

for agreeing to restrain trade in violation of the Nation's antitrust laws. *See, e.g.*, *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 505-11 (1988) (National Electrical Code of acceptable electrical products authored by private, stakeholder association subject to Sherman Act; not immune under *Noerr-Pennington* doctrine); *Radiant Burners, Inc. v. Peoples Gas Light and Coke Co.*, 364 U.S. 656, 659-60 (1961) (private natural gas association that set standards for gas burning equipment not immune from Sherman Act liability); *Consolidated Metal Products, Inc. v. American Petroleum Institute*, 846 F.2d 284, 289 (5th Cir. 1988) (private trade association that evaluates products and issues opinions subject to rule of reason under Sherman Act). Second, neither FERC nor any other governmental body with enforcement authority can delegate enforcement and sanctioning authority to a private standard-setting organization, such as NERC and the regional councils, without its actions being challenged on the ground that the organization is usurping Congress' authority to legislate, in violation of Article I of the Constitution. One solution would have been for Congress to authorize a self-regulating, private standard setting and enforcing organization. The NOI refers to such a legislative proposal. As part of an industry stakeholder group, EPMI helped to draft a legislative provision, included in the Administration's Comprehensive Electricity Competition Act ("CECA"), that would have established procedures for the creation and operation of a private self-regulating electric reliability organization ("ERO"), together with affiliated regional reliability organizations. The ERO would have possessed authority to prescribe and enforce, subject to FERC review, mandatory reliability standards. That effort, however, did not result in legislation, and (as the Department apparently recognizes) neither CECA nor this provision of its are likely to see Congressional enactment soon. That reality, however, in no sense diminishes the industry's need for uniform and enforceable reliability standards. The alternative is a rulemaking, such as the Department is proposing.

At the time that industry stakeholders negotiated and the Administration proposed the Electric Reliability title of CECA (Title VI), FERC had yet to adopt its Order No. 2000 on RTOs. That Order found that the current distribution of operational control of the bulk power system fails to achieve economic and engineering efficiencies and remains vulnerable to undue discrimination by the vertically integrated utility owners of the interstate grid. As a remedy, Order No. 2000 set deadlines for TOPUs to submit to FERC voluntary proposals to reconfigure themselves into RTOs that possess four characteristics and are capable of performing eight minimum functions. Among other things, RTOs are charged with responsibility for the short-term reliability (security) of the bulk power system.

Because the Order No. 2000 program was not mandatory and because participation in an RTO would deprive TOPUs of lucrative opportunities to use their transmission systems to discriminate in favor of their own or affiliated electricity sales opportunities, subscription to the RTO program has been (to say the least) lackluster. While not surprising, this is disappointing because, in the absence of legislation authorizing an ERO, the formation of five or six RTOs to operate the Nation's bulk power system offers the best vehicle for producing uniform reliability standards that could be enforceable by FERC.

For this reason, EPMI recommends that the Department make central to its rulemaking an RTO program in which participation is compulsory by the end of 2001. The rulemaking should make findings as to the appropriate scope and configuration of RTOs. They should be as geographically large as feasible; their number should be few, no more than ten.[3] This discrete and manageable number of RTOs — as opposed to the hundred-plus existing TOPUs and other transmission owners —could be charged with

[3]There are currently 10 regional reliability councils within the North American Electric Reliability Council. These existing councils could possibly be the starting point for RTO formation and could be further consolidated over time.

working with NERC and the appropriate regional organizations to develop and recommend for FERC approval a set of uniform reliability standards.[4] Thereafter, standards ultimately approved by FERC, following public notice and comment under FPA procedures, would be made part of each RTO's open-access transmission tariff ("OATT") on file with FERC.[5] Because the standards would be part of a public utility's schedule of terms and conditions of service under the FPA, they would be fully enforceable against any user of the bulk power system, including the interstate transmission grid. *E.g., Keogh v. Chicago & Northwestern Railway Co.*, 260 U.S. 156, 163 (1922) ("legal rights of shipper as against carrier . . . are measured by the published tariff"). While this may be administratively more complex than direct enforcement by an ERO, subject only to FERC oversight, it does the job until such time as Congress authorizes an ERO.[6]

III.
VOLUNTARY STANDARDS CANNOT ENSURE RELIABILITY OF THE BULK POWER TRANSMISSION SYSTEM
(NOI Question 1)

[4]In this capacity, the RTOs would be petitioning an administrative arm of government to adopt standards that may have an effect on competition. This petitioning would be protected from antitrust liability under the *Noerr-Pennington* doctrine. *See Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 136-7 (1961) (association seeking legislation with competitive impact held immune); *United Mine Workers v. Pennington*, 381 U.S. 657, 669 (1965) (extending *Noerr* petitioning immunity to efforts to influence administrative process).

[5]Pending RTO formation and the development of RTO standards, the Department could direct NERC to file with FERC those of its existing standards that it believes should become part of every TOPU's tariff. Those standards accepted by FERC would become part of the NERC tariff that was placed on file with FERC in order to implement NERC's transmission loading relief ("TLR") procedures. Following the practice developed in connection with the TLR procedures, all TOPUs could then be instructed to adopt the NERC standards.

[6]EPMI is not contending that the formation of RTOs and their recommendation of reliability standards obviates the need in the long-term for legislation authorizing a self-regulating organization with the power to set and enforce reliability standards. Rather, we are simply recommending an effective way of getting enforceable standards in place, pending enactment of the required legislation.

Continued reliance on voluntary compliance with industry reliability standards is unlikely to preserve the stability and security of the bulk power transmission grid. Instead, the industry needs an independent authority, not beholden to any commercial interest in the power industry, that possesses the expertise to develop uniform reliability standards for operation of the interconnected North America bulk power system. There is evidence from the past two summers that transmission operators, during periods of high prices, violated reliability rules in order to make up (*i.e.*, steal from the grid) shortfalls in power they had contracted to deliver.

Why is voluntary compliance insufficient? There are two principal reasons. First, the operators of today's grid, with few exceptions, are also merchant suppliers in the increasingly competitive bulk and retail power markets. Their irresistible incentive is to operate the grid and interpret voluntary reliability standards in inefficient ways, intended to favor their commercial interests and discriminate against their competitors. FERC has twice determined that this incentive is inherent in vertical integration of transmission with sales activities.[7] The operator's incentive to discriminate in this manner has a Balkanizing effect on the grid, cutting

[7]This determination was made in both FERC's open-access transmission order, *Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. ¶ 31,036 at 31,683(1996)[hereinafter cited as *Order No. 888*] , *clarified*, 76 F.E.R.C. ¶¶ 61,009, 61,347 (1996), *order on reh'g*, Order No. 888-A, III F.E.R.C. Stats. & Regs. ¶ 31,048 at 30,210 (1997)[hereinafter cited as *Order No. 888-A*], *order on reh'g*, Order No. 888-B, 81 F.E.R.C. ¶ 61,248 (1997), *aff'd and remanded sub nom. Transmission Access Policy Study Group v. FERC*, 225 F.3d 667 (D.C. Cir. 2000), *petition for cert. filed sub nom. People of the State of New York and Public Serv. Comm. of the State of New York v. FERC*, 69 U.S.L.W. 3281 (U.S. Oct. 11, 2000) (No. 00-568), and its order promoting RTOS, *Regional Transmission Organizations*, Order No. 2000, [1996 - 2000 Regs. Preambles] III F.E.R.C. Stats. & Regs. ¶ 31,089 at 31,004 (2000) [hereinafter cited as *Order No. 2000*], *order on reh'g*, Order No. 2000-A, III F.E.R.C. Stats. & Regs. ¶ 31,092 (2000), *appeal docketed sub nom. Public Utility District No. 1 of Snohomish County, Washington v. FERC*, Nos. 00-1174, *et al.*, (D.C. Cir. April 24, 2000).

off system operators' access to resources that would otherwise be available to aid in securing the bulk power system.

Examples of discrimination are legion. NERC TLR is a good illustration. TLR is a sequence of procedures used by security coordinators (who typically also are vertically integrated utilities) for initially cutting off new schedules for use of the transmission grid and ultimately cutting existing schedules if necessary to prevent thermal overloading of transmission lines. As a last-resort form of rationing that should be resorted to only after re-dispatch options have been exhausted, TLR should be implemented in response to operational realities rather than to achieve commercial advantage. During the past two turbulent summers, when demand soared and lines were heavily loaded, security coordinators were observed on several occasions to exercise their discretion to freeze or cut their competitors' schedules but not their own or their affiliate's. This was the case even though all of the schedules were flowing on the same path and contributing equally to the overloading of transmission lines in question.

Control area operations is another good example in which competitive sellers perceive that vertically integrated utilities are allowed to establish reliability rules that favor their own commercial interest and disadvantage their competitors. NERC's voluntary operating policies call for the creation of control areas and control area operators.[8] A control area is an electrical system that, through metering and telemetry at

[8]In fairness to NERC, it should be noted that the organization has recognized the conflict of interest that is created when either a security coordinator or a control area operator is also a vertically integrated TOPU. To date, however, the organization has been prevented by TOPUs from requiring that security coordinators and control area operators be independent. This issue will be before the NERC Board at its February 2001 meeting. RTO formation can solve both conflicts. FERC already requires that the RTO be its region's security coordinator. Further, while Order No. 2000 does not require that the RTO supplant all control areas within its region, the RTO could easily be required to confine pre-existing control areas to managing area control error and to take over scheduling to ensure that scheduling rights are equal for all users.

its borders with a neighboring system, is capable of (1) controlling directly and continuously its own generation so that it can balance its schedule and actual power transfers with its neighbors (interchange) and (2) helping the larger interconnection (of which it is a part) to stabilize alternating-current frequency. While these functions are directly related to maintaining the security of the grid, they confer on vertically integrated utilities, which ordinarily are their own control area, the ability to discriminate in favor of their own commercial interests and against competitors. As part of its duty to balance schedules, control area operators are allowed to schedule transmission of power into the region that they serve before they know where they will ultimately deliver the power. This allows the control area or its affiliates to take a commercial position in the market — *i.e.*, tie up some supply and transmission into a market before it has buyers. Most control areas deny this flexibility to their non-vertically integrated competitors, even those that possess all of the metered generation and telemetry capabilities of a control area operator. *See, e.g.*, *Entergy Services, Inc.*, 91 F.E.R.C. ¶ 61,151 (2000), *order on reh'g*, 92 F.E.R.C. ¶ 61,108 (2000). This deprives the control-area of resources that could be used to perform reliability functions if the competitive supplier were permitted likewise to take a position in the market.

In summary, creation of RTOs would go a long way toward ensuring the security of the bulk power system in a competitive environment. It would place the operational control of the interstate grid in the hands of a few fully independent operators, guided only by their interest in securing the system. They would jointly develop uniform standards and, through FERC, enforce the standards fairly and evenly.

IV.
UNDER EXISTING AUTHORITIES, FERC CAN MAKE BOTH STRUCTURAL AND POLICY CHANGES THAT ADDRESS RELIABILITY CONCERNS (NOI Question 2)

FERC's immediate options are somewhat limited by the fact that, under the FPA, FERC operates principally as an economic regulatory authority and its expertise is similarly confined. It does not have the expertise to evaluate and select among competing engineering standards for secure operations. Notwithstanding these limitations, FERC can quickly and effectively address reliability concerns in a competitive market context. It can do so through RTOs, NERC and the various regional councils of NERC that do possess the operational expertise to set reliability standards. But first RTOs must be required to be formed. Once in place, the RTOs (working in conjunction with NERC and the regional councils) can be charged with assembling and proposing to FERC the standards that they need to have in place in order to operate securely the interstate transmission grid. Pending RTO formation and adoption of RTO standards, NERC and the regional councils can perform this function by proposing for FERC adoption of certain of their existing reliability standards.

A. RTOs Should Be Directed to Apply Transparent Open-Access Rules to All Uses of the Interstate Transmission Grid

In its open-access transmission order, Order No. 888, FERC found that complete open access to all of the interstate transmission grid and services would not only benefit consumers with lower prices, but would also improve reliability by permitting the free flow of energy and the ancillary services that are

required to keep the grid operations stable and secure.[9] This finding is also central to FERC's Order No. 2000, which asks TOPUs to volunteer the operational control of their transmission systems to an RTO responsible, among other things, for short-term reliability.[10] Despite this finding and its significance to reliability, FERC has made only a small fraction of the uses of the interstate grid subject to a transparent OATT. It exempted from open access the 80-to-85 percent of grid traffic that is TOPUs delivering power to their captive retail customers because it concluded it did not have jurisdiction over these uses of the interstate grid. Moreover, it has persisted in the wishful thinking that TOPUs are going to voluntarily relinquish their ability to profit from leveraging their transmission monopoly to the advantage of their commercial power supply businesses.

The United States Court of Appeals for the District of Columbia Circuit recently affirmed nearly every aspect of Order No. 888, including its very limited application of unbundling. The Court, however, disagreed with FERC on the issue of the scope of its jurisdictional authority to order unbundling and indicated that FERC is empowered by the FPA to separate and unbundle all power supply activities from the operation of the wires, whether wholesale or retail, in order to promote competition and eliminate the incentive of vertically integrated transmission owners to discriminate in favor of their own power supply activities.

On August 31, the Court denied requests for rehearing. As a result, FERC now has authority to issue further rulings in the Order No. 888 proceeding. In its rulemaking, the Department should direct

[9] *Order No. 888*, [1991-96 Reg. Preambles] F.E.R.C. Stats. & Regs. at 31,705 (1996) (open access to ancillary services essential to maintaining reliability) .

[10] *Order No. 2000*, [1996 - 2000 Regs. Preambles] III F.E.R.C. Stats. & Regs. at 30,993 (absence of competitive open access "depriving the Nation of the benefits of lower prices and enhanced reliability"), 31,005, 31,017 (perception that access is not open or discriminatory can "harm reliability").

FERC to take the occasion of the court's decision to reopen and reconsider the Order No. 888 proceedings in order to:

- Direct each TOPU immediately to unbundle all transmission operations from power supply, including transmission bundled with retail sales.
- Apply its open-access requirement to all transmission uses, including uses bundled with retail sales.
- Direct each jurisdictional TOPU to commit the operation of that system to an RTO within one year.
- Require all RTOs to offer transmission rights that are uniform, nondiscriminatory and tradable among their holders in secondary markets, without prior regulatory approval.
- Require all RTOs to coordinate among each other so that power flows between RTOs are not impeded unnecessarily by "seams."[11]
- Expand on its decision that generator interconnection is subject to open-access principles[12] and prescribe uniform and fair rules for prompt interconnection of new, competitive generators.

The principal advantage of implementing these reforms in the context of FERC's Order No. 888 is timeliness. A proceeding is already open. In that proceeding, the steps outlined here could be implemented within a matter of months, based on an existing rulemaking record, and be in place before next summer's peak power consumption period.

B. Revisit a Uniform Capacity Reservation Approach to Selling and Buying Transmission Service

[11] Interregional coordination is a function that Order No. 2000 requires of an RTO. Even among those TOPUs that have submitted RTO formation plans to FERC, progress on interregional coordination has been disappointing.

[12] *See Central Maine Power Co.*, 90 F.E.R.C. ¶ 61,214, at 61,707 (2000), *order on reh'g*, 92 F.E.R.C. ¶ 61,054 (2000); *Tennessee Power Co.*, 90 F.E.R.C. ¶ 61,238, at 61,761 (2000).

The types of transmission access that are currently offered under FERC's OATT are awkward and illiquid. This absence of liquidity in the availability of transmission means that fewer resources are available to be used in keeping the system secure. FERC can add liquidity to the transmission market by issuing a final rule in an inquiry that has been pending since 1996 in which FERC proposed to adopt a single type of transmission service based on reserved and fully tradable rights to capacity on the interstate grid.[13] A new transmission service offering could be defined and implemented within a period of nine months to one year.

Under FERC Order No. 888, a service called "network integration" transmission is the predominant transmission service; it is what a TOPU provides to itself or sells to another utility in order for that utility to deliver power to captive retail customers. This network service is said to be "load-based" because it does not confer a property interest in transmission capability, but rather guarantees that the transmission owner will integrate a certain amount of the purchaser's demand or "load" with the generating capability of the purchaser's designated power supply resources.

The problem with network transmission service is twofold. First, it is available only to load serving entities. This means that all other wholesale transmission customers must rely on point-to-point transmission service, which lacks much of the flexibility of network service. Second, because a network customer's right of access to the grid is defined in terms of the transmission customer's own peculiar customer base or "load," the service becomes idiosyncratic to the customer. It is not and cannot be a property right that can

[13]At the same time that FERC issued its rulemaking proposals that resulted in Orders No. 888 and No. 889, it also proposed something that it referred to as a capacity reservation tariff or CRT. Because the details of this proposal were not fully developed, it drew a lot of fire, both well-founded and not. Today, four years later, it is time to dust off and reexamine the CRT concept. Doing so could be an attractive option because it would eliminate the inefficient and inconsistent ways that interstate transmission service is offered today and would do so in the context of a pending rulemaking that has already been opened and received industry input.

be traded in secondary markets when the holder does not need it. This is inefficient; it prevents the emergence of a liquid secondary market in transmission.

FERC can and should revive the pending rule-making proposal. Its initial defects can be cured quickly and easily. FERC should promptly finalize a tariff that offers only one type of transmission service and that allows transmission customers to reserve physical property rights in transmission rights that are tradable in secondary markets.

C. FERC Should Continue Its Practice of Requiring the Filing of Reliability Rules that Affect Transmission Access, Thereby Making Them Enforceable by FERC

FERC can help RTOs enforce reasonable reliability rules (set by NERC or some other authority) by obligating the RTO to make the rule part of its OATT on file with FERC. Under FPA section 205(c), 16 U.S.C. § 824d(c) (1994), a public utility's "classifications, practices, and regulations affecting such rates and charges" for interstate transmission service, "together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services" are to be publicly filed with FERC. Since adoption of the OATT, FERC has taken the position that any rules or standards that a utility adopts in order to buttress reliability, which also affect interstate transmission service, cannot be self-implementing, but must instead be filed with FERC and become part of that utility's OATT. *Coalition Against Private Tariffs*, 83 F.E.R.C. ¶ 61,015 at 61,043-44 (1998).

Once part of the OATT, the reliability standards become enforceable in an action at FERC against any user of the transmission system. What is lacking is any assurance that the reliability rule or standard be a uniform one, applicable throughout the region or interconnection in which the utility operates. FERC has encouraged standardization and uniformity in reliability provisions be added to the OATT, *id.* at 61,044 (we

"encourage[] utilities to pursue national or regional approaches whenever it appears necessary to amend the terms and conditions of the [OATT] to incorporate new operating practices"), but it has not insisted on uniformity. In the Department's rulemaking, FERC should be directed to require that operators of the interstate transmission grid, including all RTOs, adopt standards that are uniform within the three North American interconnections and that all standards be included in the RTO tariffs. This will achieve both enforceability and needed regional uniformity.

V.
ABSENT AUTHORIZING LEGISLATION, FERC MAY NOT DELEGATE TO SELF REGULATING ORGANIZATIONS ITS AUTHORITY TO ESTABLISH RELIABILITY STANDARDS
(NOI Question 3)

As most reliability standards affect the rates, terms and conditions of jurisdictional transmission service for purposes of the FPA, FERC plainly has the authority under section 201 of the Act to establish and enforce such standards. As noted earlier, the issue is not so much FERC's authority, but rather its qualification as an economic regulatory agency to establish reliability rules, grounded in engineering, in the first instance. As it is presently constituted, FERC lacks the engineering expertise to serve as the body that establishes reliability standards.

FERC could delegate its FPA authority to prescribe reliability standards affecting interstate transmission, but only in a very specific context that currently does not exist and would require legislation in order to come into existence. Specifically, FERC could delegate responsibility for establishing reliability standards to a governmental body created by an act of Congress and charged with those responsibilities. Alternatively, FERC could delegate its authority to establish reliability standards to a private body, but only

if (1) a statute authorizes function of the self-regulatory organization ("SRO"); (ii) the body is independent and complies with the process; and (iii) there is adequate agency oversight of enforcement and rulemaking functions. If these conditions are not strictly adhered to, then any private delegation of a law making function, such as standard setting, would be a delegation of legislative authority in violation of Article I, §§ 1, 8 of the U.S. Constitution. *See, e.g., Schecter Poultry Corp. v. United States*, 295 U.S. 495, 529-42 (1935) (delegation of "code of fair competition" unlawful because private body would set code to serve their own interests at expense of consumers). Even in cases where there has been an express statutory authorization of a delegation — which there has not been in the case of FERC authority to establish reliability rules — the courts have found unlawful delegations of unfettered power to private bodies. *Washington ex rel. Seattle Title Trust Co. v. Roberge*, 278 U.S. 116, 121-22(1928); *Grendel's Den v. Goodwin*, 662 F.2d 88, 92-93 (1st Cir. 1981), *aff'd sub nom. Larkin v. Grendel's Den, Inc.*, 459 U.S. 116 (1982); *State Board of Dry Cleaners v. Thrift -D-Lux Cleaners*, 254 P.2d 29, 36 (Cal. 1953).

Legal prohibitions against delegation should apply with particular force to the power industry as it is currently configured. Central to the prohibition is the point emphasized by the Supreme Court in *Carter v. Carter Coal Co.*, 298 U.S. 238 (1936): Delegation to a private body is "delegation in its most obnoxious form; for it is not even delegation to an official or an official body, presumptively disinterested, but to private persons whose interests may be and often are adverse to the interests of others in the same business." *Id*. at 311. That is precisely the problem with NERC and its regional councils. Although NERC has made its membership more inclusive in recent years, it and its regional councils remain dominated by vertically integrated utilities whose interests are adverse to all other competitive power suppliers.

In order for a delegation of FERC's authority to be lawful there would need to be legislation, such as that proposed in CECA, authorizing the delegation to a private association. The relationship between the association and FERC would need to be similar to the relationship between the National Association of Securities Dealers ("NASD") and the Securities and Exchange Commission. The hallmarks of that relationship would be that FERC would have (1) clearly delineated statutory authority to approve or disapprove the association's reliability standards, (2) authority to make *de novo* findings with respect to whether they are just and reasonable under the FPA, and (3) jurisdiction to review all of the association's decisions, including enforcement decisions. *See R. H. Johnson & Co. v. SEC*, 198 F.2d 690, 694-95 (2nd Cir.) (finding the Maloney Act delegation of SEC authority to self-regulating NASD constitutional), *cert. denied*, 344 U.S. 855 (1952); *Todd and Co., Inc. v. SEC*, 557 F.2d 1008, 1012 (3rd Cir. 1977) (same).

Until there is legislation, the Department should direct FERC to proceed on two fronts. In the immediate term, FERC should direct NERC and the regional councils to file with FERC proposed reliability standards for each of the three interconnections. FERC should accept those that are just and reasonable under the FPA and require all TOPU's within each interconnection to include the standards in their OATT. Concurrently, FERC should proceed with compulsory RTO development, including the development of RTO reliability standards to be included in RTO transmission tariffs, where they can be enforced by FERC.

VI.
THE COMPREHENSIVE ELECTRICITY COMPETITION ACT (H.R. 1828; S. 1047) CONTEMPLATED CONGRESSIONAL AUTHORIZATION OF AN ERO & IS OF LIMITED VALUE IN THE ABSENCE OF AN ERO
(NOI Question 4)

Title VI of the Comprehensive Electricity Competition Act ("CECA") was designed specifically to create legislatively an ERO using the NASD model. Without the enabling legislation, the Department and FERC will have to proceed under existing authorities to put in place enforceable reliability rules. The provisions of CECA will be of little relevance.

Independent of CECA, however, there are important reliability initiatives that can be pursued in one or more rulemakings. As explained earlier in response to question 2, FERC has existing rulemaking dockets open in which it could (1) apply open access and the OATT to all uses of the interstate grid, (2) mandate RTO participation by all transmission-owning public utilities, (3) adopt a single reservation-based form of transmission service offering, and (4) cause reliability standards to be included in RTO transmission tariffs where they will be enforceable by FERC. With those reforms implemented, the Department or FERC could direct the resulting RTOs to propose uniform reliability rules for the region. As the RTO would be independent of any commercial interests in the power industry, FERC could properly show deference to the RTO's proposal, without the risk that its actions be perceived as an unconstitutional delegation.

VII.
IF AN ERO AS PROPOSED IN CECA COMES INTO EXISTENCE, THEN IT WOULD SET RELIABILITY STANDARDS THAT THE RTOS WOULD IMPLEMENT (NOI Question 5)

CECA contemplates an ERO that would set uniform reliability standards for the interconnected North America grid and enforce them, subject to FERC review in the U.S. and provincial or federal review in Canada and Mexico, respectively. Order No. 2000 demands of an RTO that it be responsible for short-term reliability of the transmission system that it operates. In terms of the relationship between these two entities, the ERO then would set and enforce the standard for short-term reliability (security) and the RTO implement those standards in its region.

In this relationship, having one set of uniform reliability standards across RTOs is critically important. Indeed, it is just as important as is having one set of rules for securing access to the interstate grid. This is because power is bought and sold across regions, particularly when the time of peak consumption is different between regions. Failure to achieve uniformity introduces "seams" into the interconnected transmission system, which impedes the free flow of power. Uniform reliability standards, in contrast, will facilitate the transmission and exchange between regions of ancillary services that are essential to stable and secure operations. Because of this need for uniformity, when and if legislation authorizing an ERO is enacted, it is important that it, and not a regional subordinate, be tasked with originating the reliability standards. Similarly, if it is the RTO that originates the standards, in the absence of an ERO, FERC should be directed to go beyond requesting uniformity to insisting upon it, consistent with the potentially differing needs of each of the three interconnections.

VIII.
THE DEPARTMENT'S RULEMAKING SHOULD RECOGNIZE THAT THE BULK POWER MARKET & INTERCONNECTED GRID ARE MATTERS OF INTERSTATE COMMERCE REQUIRING FEDERAL SOLUTIONS
(NOI Question 6)

If the Department acts under section 403 of the DOE Organization Act to initiate an electric reliability rulemaking at FERC, then it would behoove the Department to emphasize to both FERC and State authorities precisely what the objective of the rulemaking is. If it puts in place a process for establishing reliability standards that can be enforced by FERC, then both FERC and the State authorities need to be put on notice that there is to be one uniform set of standards and not one for each of the contiguous 48 states.

As contemplated in CECA, the process prescribed for setting standards ensured their uniformity. Specifically, the ERO was called upon to propose reliability standards to FERC. If any interested party thereafter objected to a standard, then it could seek a variance from the ERO, with a right of appeal to FERC. A granted variance would become a standard. At the heart of this process, however, all standards would originate with the ERO. In the absence of an ERO, FERC should seek industry recommendations on, and then propose reliability standards in a notice of proposed rulemaking. Once the standards are finalized, they should be uniform for all regions and any RTO or other transmission operator should not be able to deviate from the standards without first securing a variance from FERC.

The role for State authorities should consist of participating and advising on the formation of RTOs — their inclusiveness and the propriety for their scope and configuration, being a commenter, first in recommending standards to FERC and later in commenting on FERC's. In addition, State authorities can and should work with their RTOs to ensure that the standards that they propose are complete and workable.

However, in the service of uniformity, no State should have authority unilaterally to establish reliability rules for that portion of the interstate grid that lies within its borders. Any greater role for States should be viewed with skepticism because inconsistent rules from State to State would have a Balkanizing and destabilizing impact on the operation of the interstate grid.

IX.
CANADIAN, MEXICAN & U.S. INTERESTS IN RELIABILITY STANDARDS SHOULD BE COORDINATED THROUGH EXISTING TREATIES & AGREEMENTS (NOI Question 7)

CECA contemplated that the ERO would seek recognition from all three North American governments. In the absence of legislation authorizing an ERO in this country, existing treaties and agreements will need to provide the framework for international coordination in how the three governments set and enforce reliability standards for the North American interconnected grid. In the short-term, the Department could recommend to its counterpart(s) in Canada and Mexico, that they proceed, as recommended here, by asking NERC (whose members include TOPUs in both Canada and Mexico) to submit for inclusion in enforceable tariffs those reliability rules that require enforceability in order to ensure the security of the interconnected transmission system.

To ensure full North American coordination in the long term, however, some more formal treaty or agreement should be pursued. The most likely vehicle for such an agreement is the North American Free Trade Agreement ("NAFTA") between Canada, Mexico and the U.S. In its current form, NAFTA has only limited applicability to the Mexican electric power sector. This is because Chapter 6, dealing with Energy and Basic Petrochemicals, expressly reserves to the Mexican State investment in and provision of "electricity

as a public service in Mexico, including . . . the generation transmission, transformation, distribution and sale of electricity." NAFTA, Chap. 6, Annex 602.3.[14] Notwithstanding this subject matter limitation, chapter 9 of NAFTA — Standards-Related Measures — is a framework within which the Parties can "promote the compatibility of a specific standard or conformity assessment procedure." *Id.* Chap. 9, Art. 906(3). By using the NAFTA framework, the Parties can meet in subcommittees or working groups, under the Committee on Standards-Related Measures, and establish enforceable international standards. Subcommittees or working groups operating under the Committee on Standards-Related Measures specifically contemplate inclusion of the types of non-governmental bodies, scientists, and technical experts that would be essential to the development of reliability standards. *Id.* Chap. 9, Art. 913(4).

NAFTA currently contains a chapter on Telecommunications that includes standards-related measures for the attachment of terminal or other equipments to public telecommunications transport networks. *Id.* Chap. 13, Art. 1301(c). Because the bulk power market and interconnected transmission grid is a network industry like telecommunications, this chapter could serve as a model for a new chapter for electricity transmission pursuant to which procedures for establishing and enforcing North American reliability standard could be established.[15]

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[14]Chapter 6 carves out limited exceptions to this general rule, which permit enterprises of a Party to acquire, establish and/or operate in Mexico "within-the-fence" generation, cogeneration, and merchant plants and sell any excess power to the Comisión Federal de Electricidad ("CFE"). The former two may sell their output to their industrial/commercial host and to CFE, while merchant plants must sell all of their output at wholesale to CFE.

[15]Various directives of the Commission of the European Communities ("CEC") might also prove instructive. For example, currently the Commission is developing CEC-wide standards for another network industry, the passenger rail system, which include standards on signaling, command and control systems, and a new standard telecommunications carrier for the railways. *See Communication from the Commission on Integrating Conventional Rail Systems — Directive of the European Parliament and the Council on the Interoperability of the Trans-European Conventional Rail System* (Nov. 25, 1999).

X.
CONCLUSION

For the foregoing reasons, EPMI urges the Department to proceed from this NOI to a rule-making, consistent with these comments and answers, to help the industry develop the new policies and structures needed to maintain security in a competitively restructured industry.

Respectfully submitted,

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